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U.S. FOREIGN ECONOMIC POLICY OUTLOOK: THE VIEW FROM CAPITOL HILL

Summary

With passage of the 1988 Omnibus Trade and Competitiveness Act last August, Capitol Hill has turned its attention to issues that are more domestically focused. Yet as the search for ways to lower both the budget and the trade deficits goes on, lawmakers continue to express concern about the question of American competitiveness. The concept of economic security also is of increasing importance to legislators, who are writing legislation to help America meet international challengers. Helping the links between trade and defense to become more intertwined is a thaw in East-West relations, which allows Washington to concentrate on bolstering America's means to compete. This is taking place against a background in which shifts in trading patterns away from Europe and toward the growing economies in Asia has the United States reassessing the ways in which both it and its partners conduct trade. Thus, while trade matters do not have the same prominence in Congress this year that they had in 1988, the trade issue is inherent in much of the economic policy debate on Capitol Hill.

Overview

Congress last year focused on successful passage of the 1988 Omnibus Trade and Competitiveness Act. By contrast, the first session of the current Congress so far has been consumed by the issue of ethics in various forms -- the Senate with its critical examination of Secretary of Defense nominee John Tower and the House with its concerns over misconduct charges against Speaker Jim Wright (D, Tex.) and the personal finances of Majority Whip Tony Coelho (D,

Calif.). Recently returned from the Fourth of July recess and with new democratic leadership in the House, Congress appears anxious to move forward with previously stalled matters.

Dominating current Capitol Hill concerns are such domestic problems as the savings and loan crisis and health care. These traditionally Democratic issues were simmering on the back burner during the Reagan years. Another key issue is the federal budget deficit. President Bush still does not want to raise taxes. The possibility of invoking provisions of the Gramm-Rudman-Hollings act to force a reduction in the deficit looms ahead. In hearings that began in July the appropriations committees have been trying to pare down authorizations.

With the current thaw in East-West relations and with arms control talks moving forward, the Bush administration, like Congress, is turning its attention to domestic issues, leaving the defense build-up that was a key priority of the Reagan White House to compete for funding with other areas on the budget-balancing scale. Nevertheless, the interplay between the administration and Congress over various domestic and foreign policy issues continues to keep trade and defense among Washington's top concerns.

Trade Bill

Congress spent over three years hammering out the details of the 1988 trade act. The process was slow and painful as amendments were offered, accepted or rejected. Much energy was expended on creating a bill that could gain enough support to pass in both houses and that was acceptable to the Reagan administration. Contentious amendments were proposed, often falling to defeat or being reshaped after vociferous debates. Among these were one sponsored by Rep. Richard Gephardt (D, Mo.) to penalize trade partners that run consistent trade surpluses with the United States and one by Rep. John Bryant (D, Tex.) to require more detailed information on foreign direct investment in this country (see JEI Report No. 38A, October 7, 1989).

Since passage of the 1988 trade act last August, legislators have been watching to see how the executive branch implements the measure. A number of trade oversight hearings on both sides of the Hill help Congress keep in touch with the various steps taken under the trade act. Only if a gap in policy appears are major new trade bills likely to materialize.

Free-trader Rep. Bill Frenzel (R, Minn.), a member of the trade subcommittee of the House Ways and Means Committee, which oversees administration of the trade act, believes that Congress lacks the energy for a new round of trade legislation. He adds that at this point no one wants to risk undermining the trade act on which Congress expended so much energy by crafting new measures. Mr. Frenzel said at an international economics conference in May that although he does not like the legislation, now that it is law, he would like to see it employed as effectively as possible. For the law to have persuasive powers with American trade partners, he said, U.S. policymakers need to stand behind the measure.

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Several legislators appear to be standing very close, watching the progress being made by U.S. Trade Representative Carla Hills and her staff on investigations and negotiations mandated by the trade act. So far Ms. Hills is winning their confidence (see JEI Report No. 24B, June 23, 1989). Following the letter of the law, USTR Hills identified U.S. trade-liberalization priorities and countries before the May 30 deadline. At the top of the list, responding to the strong sentiments of some in Congress, was Japan, cited for barriers to imports in three areas: government procurement of supercomputers and satellites and technical standards for wood products (see JEI Report No. 22B, June 9, 1989). Sens. Lloyd Bentsen (D, Tex.), chairman of the Senate Finance Committee, and John Danforth (R, Mo.) were outspoken about their desire to have Japan named. Sen. Danforth told Ms. Hills during hearings that the provision of the trade law dubbed Super 301 had been written specifically with Japan in mind.

Named along with Japan were Brazil for import restrictions that limit purchases of agricultural and manufactured products from abroad and India for barriers to insurance and performance requirements for foreign investment. All three countries have balked at being named and have tried to get international opinion to condemn the U.S. action. While Japan has agreed to enter trade talks with Washington, Tokyo has refused to negotiate under the Super 301 framework.

Also being watched closely in Congress is Japan's reaction to the White House's proposal of separate structural-adjustment negotiations, talks designed to get at the heart of generic or systemic Japanese trade barriers. Japan's distribution system is one such issue. Many in the administration and the American business community have pressed Tokyo to repeal the Large Retail Store Law, which they feel limits the growth of imports by making it difficult for big retailers -- the stores most likely to handle foreign-made products -- to expand (see JEI Reports No. 11A, March 17, 1989, and No. 24B, June 23, 1989).

The structural impediment talks are expected to be much more difficult than the negotiations on supercomputers, satellites and wood products. But these discussions may yield more long-term benefits for U.S. exporters by getting at problems that affect American competitors across-the-board. The international trade subcommittee of the Senate Finance Committee has scheduled initial hearings on the structural-adjustment initiative for July 20.

Oversight of these talks may be intermittent as Congress turns its attention to matters ignored when it was preoccupied by ethics charges and as Japan deals with its own domestic problems, including the political damages caused by the Recruit Co., Ltd. influence-buying scandal, which tainted most of the first tiers of leadership and toppled the government of former Prime Minister Noboru Takeshita. Japanese politicians are busy campaigning for the July 23 upper house elections, which offer the opposition parties collectively a chance to gain their first majority since Liberal Democratic Party dominance began in 1955. Progress on trade talks between the United States and Japan apparently will be left in the hands of bureaucrats.

New Directions for Legislation

A new direction in economic legislation, less directly linked with trade, may begin to emphasize ways to bolster American competitiveness. This is the type of legislation being discussed in the case of high-definition

television, for example. Much of it involves shifts in government policies, including exemptions to antitrust laws to allow American companies to team up to manufacture and market in addition to doing joint research and development.

Legislators are concerned not only with America being behind Japan in the development of many cutting-edge technologies, such as HDTV, but with the long-term implications of this trend as well. Having seen foreign competitiors take technologies developed in the United States and commercialize them, such as what happened with videocassette recorders, lawmakers are leery of Japan or other countries moving too far ahead technologically.

Missed U.S. market opportunities are not the only reason for congressional concern about the competitiveness of American industry. The technologies discovered in the process of designing and developing a product may be more important than the product itself. HDTV technologies and their implications for the embattled semiconductor industry are a case in point. To many congressmen the potential spin-offs from HDTV research and development justify at least some direct government funding for this work (se JEI Report No. 19B, May 12, 1989). A precedent already exists. Congress appropriated $100 million for FY 1989 for the Sematech R&D consortium in the belief that the health of such an industry as semiconductors is vital to the defense industrial base and thus the security of the United States.

The linkages increasingly drawn on Capitol Hill between trade and defense were seen most clearly this spring during the fight over the FSX, Japan's next-generation fighter support aircraft (see JEI Report No. 21A, May 26, 1989). Many legislators no longer believe that the nation's military and economic security can be separated. In the FSX debate the major concern was not about losing military secrets to Japan but rather how the knowledge Japanese industry gained through the deal would find commercial applications.

Congress also has become more vocal about what it sees as the inequitable amounts of money the United States and its allies spend on world military security. This has become a pointed issue in regard to Japan, which is limited by its constitution to defensive outlays only. Tokyo also has followed a self-imposed ceiling of spending approximately 1 percent of GNP on defense.

Japan's decision to make official development assistance its major contribution to global security has raised another issue: powersharing. While willing to assume some military security burdens through foreign aid contributions, Japan would like to get greater recognition of its economic contributions by receiving more of a say in the leadership of international organizations that handle aid. It is unclear, however, whether Congress and the administration are willing to exchange powersharing for burdensharing. Between its foreign aid and its defense budget Japan spends approximately 1.32 percent of its gross national product on allied security -- a proportion that is considerably below the U.S. level of approximately 5 to 6 percent of GNP on defense annually and 0.2 percent in 1988 on foreign aid. This discrepancy and the problems posed by the enormous U.S. budget deficit may color future congressional debates on burdensharing and powersharing.

Shifting Trade Patterns

In the meantime, the traditional U.S. bent toward Europe is being rearranged through shifting trade winds toward Asia. Although the European

Community's 1992 integration has important implications for American businesses as they prepare for one common market, the rapid expansion of the Asian market in the 1980s has brought crucial changes in U.S. trade patterns. Along with these shifts have come sizable trade deficits, not only with Japan but also with a number of Asia's newly industrialized economies, such as Taiwan and South Korea (see Table).

The altered trade patterns suggest a new set of priorities for the United States. When the Asian nations were considered less developed countries, Congress and the administration were not overly concerned with how effectively international trade laws were enforced. Infractions or blatant disregard for international trade norms could be overlooked due to the low levels of trade. Now that these economies are growing exporters and have the potential to be important markets for U.S. suppliers of goods and services, people at both ends of Pennsylvania Avenue believe the United States can no longer afford such lenient attitudes.

Washington, for example, has become increasingly concerned about inadequate safeguards for intellectual property rights in some of the newly industrialized economies. Of the eight countries USTR named May 28 for priority reviews of intellectual property rights under a section of the 1988 trade law dubbed Special 301, five are Asian countries: China, India, South Korea, Taiwan and Thailand. Additionally, of the 17 countries placed on a watch list five are Asian, including Japan.

As the U.S. trade deficit mounts with Asian countries, lawmakers are certain to scrutinize the ways in which other countries improve their export competitiveness and protect their home markets. Many analysts wonder whether this concern with trade deficits will alter America's basic free-trade policies. Congress passed the 1988 trade act in order to bolster American competitiveness, but many free traders cite this law and other legislation as evidence that America is turning away from its tradition of open door, free trade and toward more protectionism. Free traders also express concern that the trade law is unilateral in nature, a shift away from the multilateral thrust of earlier U.S. trade policy. Along with major U.S. trading partners, Japan included, they have questioned whether particular sections of the legislation, notably the Super 301 measure, are consistent with the General Agreement on Tariffs and Trade.

USTR Hills has been careful to point out that the United States still stands behind the multilateral trading system and that the only unilateral action involved in the Super 301 announcement is the stating of U.S. priorities for trade negotiations. In fact, in announcing the designation of Japan, Brazil and India as Super 301 targets, the chief U.S. trade negotiator stated that this country's top trade-liberalization priority is the successful completion of the Uruguay Round of multilateral trade negotiations. But progress in the talks has been slow (see JEI Report No. 25A, June 30, 1989), and Washington has used the trade bill to gain leverage over certain U.S. trading partners. For example, concessions were wrangled out of Taiwan and South Korea as each tried to remain off the Super 301 hit list. South Korea gave ground on foreign investment, agriculture, product standards, testing requirements, customs procedures and import bans designed to foster local manufacturing. Taiwan agreed to reduce tariffs and liberalize insurance and banking laws. USTR Hills believes that actions such as these are beneficial to the multilateral trading system

U.S. Trade Balance with Major Trading Partners, 1984-88

(in millions of dollars; exports f.a.s., imports c.i.f.)

	1984	1985	1986	1987	1988
Total	$-123,289	$-148,480	$-169,777	$-171,217	$-139,539
Western Hemisphere	-40,766	-40,252	-36,364	-25,810	-21,981
Canada	-20,387	-22,176	-23,330	-11,696	-12,201
Mexico	-6,275	-5,757	-5,167	-5,938	2,901
Brazil	-5,633	-5,007	-3,455	-4,393	-5,687
Venezuela	-3,443	-3,431	-2,305	-2,295	-968
Colombia	197	12	-720	-1,003	-591
Western Europe	-16,902	-27,446	-32,655	-30,216	-17,040
United Kingdom	-2,834	-4,300	-4,614	-3,884	-337
West Germany	-8,726	-12,182	-15,568	-16,281	-13,089
Netherlands	3,224	2,901	3,485	3,981	5,221
France	-2,479	-3,864	-3,370	-3,233	-2,603
Belgium-Luxembourg	2,014	1,351	1,208	1,830	2,686
Italy	-4,129	-5,756	-6,473	-6,168	-5,495
European Community*	-13,291	-22,470	-26,366	-24,301	-12,822
Switzerland	-636	-1,291	-2,391	-1,212	-538
Spain	-66	-250	-341	47	747
Sweden	-1,885	-2,414	-2,766	-3,088	-2,512
Asia and Middle East	-63,158	-78,971	-96,031	-107,538	-96,438
Japan	-36,796	-49,749	-58,575	-59,825	-55,436
Korea	-4,044	-4,757	-7,142	-9,892	-9,920
Taiwan	-11,085	-13,061	-15,727	-18,994	-14,126
Singapore	-446	-936	-1,504	-2,342	-2,456
Hong Kong	-5,837	-6,208	-6,444	-6,507	-5,119
Saudi Arabia	1,555	2,447	-606	-1,513	-2,438
Israel	385	379	-267	406	180
Malaysia	-969	-860	-805	-1,157	-1,714
Philippines	-856	-955	-787	-882	-1,026
Thailand	-313	-694	-937	-833	-1,459
India	-1,167	-836	-928	-1,262	-669
Indonesia	-4,652	-4,138	-2,730	-2,952	-2,438
Australia and Oceania	1,860	2,229	2,578	1,976	2,943
Australia	1,894	2,372	2,679	2,208	3,125
Africa	-6,169	-5,155	-5,079	-6,396	-4,279
Egypt	2,522	2,239	1,859	1,712	2,097
South Africa	-312	-975	-1,318	-118	101
Nigeria	-2,029	-2,432	-2,272	-3,472	-3,179
Communist Countries	1,479	749	-2,322	-3,309	-2,952
China	-377	-368	-2,134	-3,413	-4,231
Soviet Union	2,684	1,980	642	1,010	2,119

*1986-88 figures include Spain and Portugal.

Source: Department of Commerce

since, once barriers to trade are removed, all countries will have better market access, not just the United States.

Also raising questions about the U.S. commitment to the multilateral trade regime is the attention being paid by Congress to free-trade agreements. As difficulties have appeared in the Uruguay Round negotiations, a number of legislators have proposed a broader context in which to resolve trade problems, most frequently some variation on a free-trade agreement. The successful conclusion of a free-trade pact with Canada and the coming integration of the European market also have spurred consideration of other partners or sets of partners for free-trade arrangements.

As the area with the largest overall amount of trade with the United States, the Far East has strong FTA candidates in either an individual country, such as Japan, or in a group of countries, such as the Association of Southeast Asian Nations (comprised of Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand). But a larger framework of economic unity, a Pacific version of the Organization for Economic Cooperation and Development, has gained in popularity among Asian countries (see JEI Report No. 26B, July 7, 1989).

Conclusion

Although Congress and the administration currently are focusing on domestic affairs, the interconnections of trade with domestic issues -- for example, the international competitive position of the United States -- make trade an important underlying concern of both branches of government. How to restore U.S. competitiveness in the world marketplace and subsequently reduce the trade deficit is one of the two major international economic issues on which Capitol Hill has been focusing in 1989, the other being implementation of the 1988 trade act. Lowering the U.S. trade deficit with Asia is the key to reducing the overall imbalance, and Congress will be monitoring the situation closely. Whether the concerns about the U.S. trade position will take Congress into new policy areas remains to be seen.

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The views expressed in this report are those of the author and do not necessarily represent those of the Japan Economic Institute.